Supreme Court of the United States.

October Term, 1940.

No. 506

A. B. & M. Liquidation Corporation,
Petitioner,
v.
Pelham Hall Company et al.,
Respondents.

A. B. & M. Liquidation Corporation,
Petitioner,
v.
Myles Standish Company et al.,
Respondents.

Petition for a Writ of Certiorari to the Circuit Court of Appeals for the First Circuit
and
Brief in Support Thereof.

RICHARD WAIT,
CHARLES P. CURTIS, JR.,
Counsel for Petitioner.

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v.

MYLES STANDISH COMPANY et al., respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT.

To the Honourable the Justices of the Supreme Court of the United States:

The undersigned, on behalf of the above-named petitioner, pray that a writ of certiorari may issue to review the judgment of the Circuit Court of Appeals for the First Circuit entered June 7, 1940, in the cases between the above-mentioned parties docketed therein as No. 3542 and No. 3543.

Opinions Below.

The opinion of the District Court is published in 28 F. Supp. 350. The opinion of the Circuit Court of Appeals is published at 112 F. (2d) 498. No opinion was announced on the denial of the petition for rehearing.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered June 7, 1940 (Rec. p. 115). A petition for rehearing was filed in the Circuit Court of Appeals on June 21, 1940, and was denied on July 15, 1940 (Rec. p. 116).

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended.

The actions to which the petition relates are bills in equity (commenced in 1937 under the old practice) in which the petitioner as holder of bonds and coupons secured by a trust mortgage seeks to share in the security and to force the issuance to it of securities in the reorganized corporations pursuant to the provisions of reorganization plans. The jurisdiction of the United States District Court where the bills were originally brought was based upon diversity of citizenship under Section 41(1) of the Judicial Code, as amended.

Statement.

From 1904 until its bankruptcy in 1931 the American Bond & Mortgage Company was engaged in the business of marketing and dealing in real estate securities.

In 1925 it was proposed to construct an apartment house in Brookline (Pelham Hall) and an apartment hotel in Boston (the Myles Standish). Two wholly distinct Massachusetts corporations, The Pelham Hall Inc. and The Myles Standish Inc., were then formed to construct and run the buildings. The funds necessary for the projects were to come from issues of bonds secured in each instance by mortgage of the property. Except for the proceeds of the sale of these bonds neither corporation had any material resources. Until the buildings were erected and tenanted there could be no source of income from which to pay either the interest or the principal (Rec. p. 48).

The bonds were to be marketed by American Bond & Mortgage Company. In each instance they were coupon bonds, bearing 6½% interest, payable semi-annually, and had serial maturities—the first two years after the date of issue. They were specifically labelled "Construction Bonds" in large red printing on their face.

Pursuant to these plans mortgage indentures (identical for all present purposes) were executed. The Myles Standish indenture was dated June 1, 1925. It provided for the issue of $1,450,000 of bonds and mortgaged the property to Harold A. Moore as individual trustee to secure the bonds and coupons (Rec. p. 44). The Pelham indenture was dated September 1, 1925. It mortgaged to the same trustee. The Pelham issue was $1,200,000 (Rec. p. 39).

The bonds were payable both as to principal and interest at the office of the American Bond & Mortgage Company in Chicago or New York, and American Bond & Mortgage Company was the paying agent of the issuer in each instance (Rec. pp. 39, 44). The funds from which it would discharge the obligation of the issuer on the first two coupons would come from moneys retained from the proceeds of sale. Thereafter the issuer was to make monthly payments of one-sixth of the interest next to fall due to American Bond & Mortgage Company. Similar payments were to be made to meet serial maturities of principal.

There was no promise by American Bond & Mortgage Company to make any payments whatsoever on behalf of the issuer out of its own funds. But although under no obligation, it was given the right to make payments by which any defaults by the issuer could be financed. This right was to purchase bonds and coupons and to hold them as outstanding (and consequently fully secured) obligations of the issuer whenever the issuer failed to make the payment due upon those bonds and coupons. This provision is

found in article II, section 3, of each indenture, which read:

> "If at any time the Company [issuer] or its assigns shall fail to pay any bond or coupon secured hereby as and when the same falls due, then American Bond & Mortgage Co., Inc. or any person, firm or corporation (when not acting for said company) may purchase and hold the same, and such bond or coupon shall not be subordinated to other outstanding bonds and coupons but shall be considered as past due obligations of the company for all purposes" (Rec. pp. 40, 41).

There was likewise a saving clause to the same effect in section 2 immediately preceding.

As things fell out each issuer did "fail to pay . . . [each] bond or coupon secured hereby as and when the same falls due." When the third coupon became due, Pelham Hall Inc. had made no payments to the American Bond & Mortgage Company. Consequently, that company exercised its option and purchased with its own funds those coupons which were presented at its offices, and the same procedure was followed on both issues with reference to each subsequent coupon maturity through December 1, 1928, in the case of the Myles Standish, and through March 1, 1929, in the case of Pelham Hall (Rec. pp. 16, 17, 79, 80).

On the early principal maturities nothing was paid by either issuer, and American Bond & Mortgage Company purchased all of the serial maturities due June 1, 1927, December 1, 1927, and June 1, 1928, of the Myles Standish Company. In the Pelham case it purchased all of the bonds maturing September 1, 1928, and March 1, 1929.

No specific notice was given by American Bond & Mortgage Company to holders of the bonds who presented coupons that it had not been put in funds by the issuer and that

it was purchasing the coupons for its own account under the provisions of the indentures. In the case of the maturing bonds which were purchased, a document known as a resale authority was sent in each instance to the party who presented the bond. The terms of these documents do not appear in the record. A large number of them were introduced in evidence in the District Court, but they were not designated by the appellants to be part of the record. They were not certified as a part nor transmitted to the Circuit Court of Appeals as separate physical exhibits with certain others. The trial judge found with reference to them:

> "The course of dealing with the bonds paid by the Mortgage Co. out of its own funds was this:
>
> "When the bond was presented for payment, the Mortgage Co. gave to the customer a 're-sale authority' or a 'customer re-sale order'. If the bonds were presented by a bank, acting for the owner or transmitted by mail, the 'authority' or 'order' was sent to the party presenting or transmitting the bond, who may or may not have been the owner. Some of these re-sale orders were signed by customers and copies retained by the Mortgage Co., but so many of them had been lost or destroyed that it was not possible to determine how many were signed by the actual owner of the bond. Without awaiting a re-sale the Mortgage Co. paid the amount of the bond, and no separate account was set up with the customer presenting the bond, or coupon, except as a matter of statistical record" (Rec. p. 49).

He also stated in his opinion:

> "All that I have said above relative to coupons is equally applicable to the matured bonds acquired by the Mortgage Co. The additional fact that the Mortgage Co., in each case, took a re-sale order from the

customer, clearly indicating an intention to purchase, is significant. These orders were notice to the customers of this intention. It is objected that the notice was not given until the bonds were received by the Mortgage Co. The bonds were not registered bonds, and it is difficult to see how the intentions of the Mortgage Co. could have been communicated to the holder until the bonds were presented for payment. In some instances the re-sale orders were signed by the holders themselves, and in others they were mailed to the party forwarding the bond. In the latter case, notice to the agent would be notice to the bondholder'' (Rec. p. 54).

As a result of all these transactions, American Bond & Mortgage Company held Myles Standish coupons amounting to $171,007.52, Myles Standish bonds amounting to $61,900 (Rec. p. 80), Pelham Hall coupons amounting to $114,255.72 and Pelham Hall bonds amounting to $30,900 (Rec. pp. 17, 18). In acquiring these it had expended its own funds and not a cent had come from the issuer in either case.

After December 1, 1928, in the Myles Standish case, and after March 1, 1929, in the Pelham Hall case, American Bond & Mortgage Company did not exercise its right to purchase the bonds and coupons, the subsequent defaults were not financed, and the properties went to foreclosure.

The Myles Standish mortgage was foreclosed May 15, 1929, and the trustee bid it in at the foreclosure sale on a bid of $1,622,391.31, which constituted the entire amount due on all bonds, coupons and other obligations secured by the mortgage, including the bonds and coupons held by American Bond & Mortgage Company. Eventually a reorganization plan was set up and made effective under which

bondholders would receive voting trust certificates of the new corporation in the proportion of one voting trust certificate for each $100 face of obligation.

In the Pelham Hall case the reorganization was put through in immediate connection with the foreclosure. The property was bought in by the straw of the reorganization committee on a bid of $450,000. The plan provided for the issuance of voting trust certificates representing one share of stock in the new corporation for each $10 face of obligation for those bondholders who had deposited their bonds.

Voting trust certificates were issued pursuant to these plans to all depositing bondholders save American Bond & Mortgage Company. As to its bonds and coupons claim was made that, although neither issuer had paid a penny toward their discharge, American Bond & Mortgage Company had paid them rather than purchased them and consequently that they could not share in the security, and the question was left to be determined by litigation.

Meanwhile American Bond & Mortgage Company itself became involved in the bad times and went into bankruptcy. The petitioner was formed as a medium for the liquidation of certain of the slow assets of the bankrupt estate for the benefit of the creditors. The Pelham and Myles Standish bonds and coupons passed to it and it commenced these suits to force the issuance to it of the voting trust certificates to which it, as holder of the bonds and coupons, was entitled under the plans. The controversy consequently was between two classes of creditors (Rec. p. 39).

The cases were heard together by Judge Brewster in the District Court. He ruled that the provisions in article II in the identures were inserted in order to allow the Mortgage Company to purchase just as it did; that those provisions were binding upon the bondholders, and that the Mortgage Company was within its rights in acting under them. He further ruled that notice to each bondholder that

it was doing so was unnecessary since otherwise the provisions would be mere surplusage, but pointed out that notice was given in the case of the bonds although not in that of the coupons (see Rec. pp. 52-55). He consequently ordered the entry of decrees in the plaintiff's favour.

The defendants other than Boston Safe Deposit & Trust Company and the interveners appealed.

The Circuit Court of Appeals for the First Circuit reversed the decree of the District Court and held that none of the bonds or coupons of either company taken up by the American Bond & Mortgage Company at or after maturity should be permitted to share in the reorganization proceedings on a parity with bonds and coupons not so taken up. The Circuit Court was of the opinion that the American Bond & Mortgage Company was under an obligation to give notice of its intention to take up matured bonds and coupons and hold them and that nothing in the provisions of the indentures freed it from this obligation. In the case of the coupons, the Circuit Court found no such notice whatsoever. In the case of the bonds, as to which the District Judge had held that the resale authorities gave constructive notice, the Circuit Court both denied the effect of the resale authorities as constructive notice and in any event held that constructive notice, even if given, was not sufficient.

The Circuit Court of Appeals sometime after the briefs had been presented and the oral argument had been completed secured from the District Court Clerk's office for its inspection the resale authorities which had been introduced in evidence in the District Court but had not been made a part of the record before the Circuit Court. The court considered the resale authorities and commented upon their terms as "somewhat vague and technical" in its opinion (Rec. p. 114). The petitioner was given no opportunity to present argument before that tribunal as to the interpretation and legal effect of these instruments.

Upon the rendition of the opinion of the Circuit Court, the petitioner filed a petition for a rehearing before that court, which petition was denied (Rec. p. 116).

Questions Presented.

Three questions are presented with respect to each case:

(1) Where securities are issued under a trust mortgage which provides that, if the issuer fails to pay any of the securities, the paying agent may purchase the same, which shall not be subordinated to other outstanding securities, and the paying agent in good faith in reliance upon that provision takes up such securities with its own money and with intent to purchase, does the fact that the paying agent in so doing fails to give notice to the holders from whom such securities are taken up that it is purchasing them require equity to treat the transaction with respect to those securities as a payment with consequent forfeiture of the money expended by the paying agent in taking them up?

(2) If on the facts stated in the preceding question failure to give the notice there referred to results in equity in forfeiture of the money advanced by the paying agent, does sending a statement indicating an intention to purchase satisfy the requirement of notice?

(3) Is it permissible for a Circuit Court of Appeals, on the basis of inspection of exhibits introduced in the District Court but not certified to the Circuit Court as a part of the record on appeal, to reverse and modify a finding by the District Judge to the effect that the statements referred to in question (2) above constituted notice?

Specification of Errors.

The Circuit Court of Appeals erred—

(1) In not giving proper effect to the decision in *Ketchum* v. *Duncan*, 96 U.S. 659.

(2) In holding that American Bond & Mortgage Company was required to give notice to bond and coupon holders that the securities which it acquired from them were being purchased and not paid, before it could be entitled to secure parity for such securities in the reorganization proceedings.

(3) In holding that the sending of a statement to bondholders, indicating an intention to purchase, did not satisfy this requirement of notice, assuming such a requirement existed.

(4) In basing its decision with respect to the parity of the bonds held by the petitioner upon the resale blanks, which did not form a part of the record on appeal and as to the interpretation and legal effect of which the petitioner was afforded no opportunity for argument.

(5) In reversing the decree of the District Court which granted the petitioner the right to have voting trust certificates of Myles Standish Company and Pelham Hall Company issued to it on a parity with all other holders of bonds and coupons.

Reasons for Granting the Writ.

1. The Circuit Court of Appeals departed from the accepted and usual course of judicial proceedings in reversing the decree of the District Court in so far as it dealt with recovery based upon bonds picked up at or after maturity through a construction of documents introduced in evidence before the District Court but not certified as a part of the record on appeal.

The record on appeal was made up strictly in accordance with the provisions of Rule 75 of the Rules of Civil Procedure. The resale authorities, so called, which the Circuit Court of Appeals construed as insufficient to constitute notice to the bondholders but which the District Court had held to constitute notice, were not included in that record. It is provided by Rule 75 with reference to the record:

> "The matter so certified and transmitted constitutes the record on appeal."

The Circuit Court of Appeals reversed the ruling made by the District Judge with reference to the resale authorities following an inspection of the original exhibits made after the conclusion of arguments without amendment of the record, without any prior notice to the petitioners, and further denied the petitioner's motion for rehearing based upon this action of the court.

Orderly procedure in the courts requires that there be no question as to the matters open to inquiry by an appellate court. It is important that this Court should determine whether a party before a Circuit Court of Appeals must anticipate decision of the appeal on the basis of material introduced before the District Court but not certified or transmitted to the Circuit Court of Appeals and consequently, within the provisions of Rule 75, not a part of the record on appeal.

2. The Circuit Court of Appeals decided an important question in the law of corporate securities in a manner which does not give the proper effect to the position of this Court in the case of *Ketchum* v. *Duncan, supra,* which is in apparent conflict with the decision of the Fifth Circuit Court of Appeals in the case of *Anderson* v. *Pennsylvania Hotel Co.,* 56 F. (2d.) 980, and which leaves the question of

the effect to be given to such applicable state court cases as *Lyman* v. *Stevens,* 123 Conn. 591, and *Chicago Title & Trust Co.* v. *Hoffberg,* 293 Ill. App. 290, completely unanswered.

It is of great importance to dealers in corporate securities acting in good faith pursuant to the provisions of an indenture governing the rights in the security to know with as much certainty as possible how far, if at all, the general law imposes additional requirements not set forth in the indenture. Substantial certainty with reference to the existence or non-existence of a requirement of notice not provided for in an indenture when a paying agent follows the common practice of picking up maturing bonds and coupons can be attained only through the decision of this Court. Until there is an authoritative decision to be followed in all circuits settling whether additional requirements will be read into the indentures, and if so, what requirements, the confusion presently existing must continue.

3. The result of the decision of the Circuit Court of Appeals is to cause the petitioner to be subjected to a forfeiture. The petitioner's predecessor had advanced its own money in order to purchase securities from certain of the bondholders and thereby enabled those bondholders to secure the face value of their securities. The petitioner is now denied the right to share in the mortgage security even at the reduced rate provided for in the plan of reorganization. This forfeiture has been enforced without any showing of prejudice to any bondholders and upon a record from which it is apparent that the bondholders benefited from the transaction. The creditors of the American Bond & Mortgage Company who would be the beneficiaries of any recovery by the petitioner in this action are in effect being compelled to donate some $325,000 to the other Myles Standish and Pelham Hall bond and coupon holders, a result which scarcely recommends itself to a court of equity.

Wherefore it is respectfully submitted that this petition shall be granted.

RICHARD WAIT,
CHARLES P. CURTIS, JR.,
Attorneys for the Petitioner.

CASSELS, POTTER & BENTLEY,
Of Counsel.

COMMONWEALTH OF MASSACHUSETTS
SUFFOLK } ss.

Richard Wait, being duly sworn, says that he is counsel for A. B. & M. Liquidation Corporation, the petitioner herein, that he prepared the foregoing petition, and that the allegations thereof are true as he verily believes.

RICHARD WAIT.

Sworn to and subscribed before me this eleventh day of October A.D. 1940.

SIMON P. TOWNSEND,
Notary Public.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

I. An important point of appellate practice is presented.

The decrees entered in the District Court gave to the petitioner recovery on account of both bonds and coupons which its predecessor had acquired with its own moneys. The District Judge ruled that no prior notice was required to be given by the petitioner's predecessor in order for the securities thus obtained by it to participate in the reorganization. But he further went on and ruled in the case of the bonds as distinct from the coupons that notice had been given through the sending of the documents designated as resale authorities. He had before him a large number of these documents which were admitted as exhibits in the District Court and characterized them as "clearly indicating an intention to purchase" (Rec. p. 54).

The Circuit Court of Appeals held the judge's ruling that no notice was necessary was wrong and that notice must have been given. That ruling left the question of participation by the bonds dependent upon the effect to be accorded to the resale authorities. The Circuit Court of Appeals held that the use of them did not satisfy the requirement of notice.

The record was made up in conformity with Rule 75 of the new Federal Rules. The parties entered into stipulations, each of which stated:

> "It is stipulated and agreed by and between the parties in the above-entitled case that the record on appeal shall consist of:"

after which some eighteen documents were listed (Rec. pp. 60 and 103). The resale authorities referred to above were not the only exhibits introduced in the District Court. Certain of the other exhibits were sent up to the Circuit Court

of Appeals physically with the record. In each case the District Judge entered an order providing:

> "It is ordered, adjudged and decreed that the clerk transmit with the record on appeal the following original exhibits to be kept with the record on appeal for inspection by the Circuit Court of Appeals" (Rec. pp. 61, 101).

These orders were entered by the consent of the parties.

The resale authorities, which, in the District Court, had been designated as Exhibits 1a through 52a, inclusive, were not listed in either stipulation as to the contents of the record, were not referred to in either order for transmission of the exhibits, and were not in fact transmitted by the Clerk of the District Court to the Circuit Court of Appeals, with the printed record on appeal.

Nevertheless the Circuit Court of Appeals, in reaching its conclusion that the resale authorities did not satisfy the requirement of notice which it had laid down, obtained the exhibits from the Clerk of the District Court, considered them, and in its opinion referred to their terms (see Rec. p. 114). This was all done after the conclusion of the oral arguments and without any prior notice to the petitioner of what was being done. After the opinion was announced the petitioner moved for a rehearing and specified as one of the grounds therefor the inspection of the resale authorities thus made. The motion was denied and in consequence the petitioner has never been accorded the opportunity, which it still desires, to argue the sufficiency of the resale authorities as constituting notice by the petitioner's predecessor.*

*This argument was made successfully in the District Court. The judge stated in his opinion: "The additional fact that the Mortgage Co., in each case, took a re-sale order from the customer, *clearly indicating an intention to purchase*, is significant. These orders were notice to the customers of this intention" (Rec. p. 54, emphasis supplied).

The provisions of Rule 75 are clear and detailed and are designed to make sure that the record on appeal shall be the one on which the appeal shall be determined. It is provided in subparagraph (g) of the rule:

> "The matter so certified and transmitted constitutes the record on appeal."

The obvious intention is that the Circuit Court of Appeals should decide the case on the matter contained in the record on appeal and upon nothing else. This is but a carrying out of the well-established rule of appellate practice.

See *Fitzgerald* v. *Evans,* 49 Fed. 426 (C.C.A. 8).
Lydiard-Peterson Co. v. *Woodman,* 205 Fed. 900 (C.C.A. 8).
Krauss Bros. Lumber Co. v. *Mellon,* 18 F. (2d) 369 (C.C.A. 5).

Cf. *Chisholm-Ryder Co.* v. *Buck,* 65 F. (2d) 735 (C.C.A. 4):

In that case the point presented was whether the appellate court could take an exhibit not offered at the trial. The following language, however, is illuminating:

> "Ever since the system of equity jurisdiction was established, it has been the settled practice that an appellate court cannot look beyond the record before it to influence its judgment . . ." (page 737).

Likewise it has been held where some substantial matter is left out of the record it is ground not for dismissal of the appeal but for affirmance of the decree appealed from.

Bank of Eureka v. *Partington,* 91 F. (2d) 587 (C.C.A. 9).

The necessity for such a rule is obvious, since arguments and briefs can scarcely be kept within any reasonable

bounds if counsel must anticipate that the court will consider documents or other evidence not contained in the record on appeal.

Had the respondents desired to argue that the resale authorities could not satisfy any requirement of notice by reason of their terms, it was open to them to have them included in the record on appeal. They did not do so. In that situation the petitioner reasonably felt justified in giving no consideration to the language of the documents and in relying upon the finding made by the District Judge with reference to them. The action of the Circuit Court of Appeals in deciding the cases as far as the bonds were concerned on the basis of an inspection of these documents has resulted in depriving the petitioner of the opportunity to argue the sufficiency of the resale authorities, an argument which it most certainly would have advanced had counsel supposed that the point was open. This action of the Circuit Court of Appeals, we submit, constituted such a departure from the accepted and usual course of judicial proceedings as to merit review by this Court.

Our argument on this point is not that under no circumstances could the Circuit Court of Appeals consider the exhibits in question. If the Circuit Court of Appeals felt that it had an incomplete record by reason of the omission of these exhibits, Rule 75(h) provides a simple method for supplying the lack, but it does not justify the denial of an opportunity to argue, which resulted from the action taken by the Circuit Court of Appeals in this case.

II. An important point of law concerning dealings with corporate securities is presented in these cases.

The basic question involved in the present litigation is not one which is of importance solely to the parties to this action but has broad implications to all those who are

owners or connected with the flotation of corporate securities, and as such merits definitive adjudication by this Court. In the previously decided cases on this subject the tendency has been to require a choice between a "purchase" and a "payment." Petitioner submits that this does not represent a true analysis of the situation. In fact, the use of the terms "purchase" and "payment" introduces into the case semantic difficulties of the worst kind.

The basic situation involves, as here, the acquisition by a paying agent under a corporate indenture of bonds and coupons at or after their respective maturities. The indenture provides that obligations not paid by the issuer may be acquired by the paying agent for its own account and when so acquired may stand on an equal footing with other outstanding obligations secured by the same indenture. The question is, then, whether a paying agent who acquires matured bonds and coupons pursuant to such indenture provisions with affirmative intent to keep them alive as valid and outstanding obligations of the issuer with rights in the mortgage security equal to other bonds and coupons in the hands of the public is to have his expectation confirmed. Or is he, because he gave no notice of his intent, to be deprived of the parity which he in good faith on the strength of the indenture provision believed to be his due, and as a consequence forced to lose his money? This loss would be forced by the implication into the indenture of a requirement that he must give notice at the time of his acquisition of the securities that he proposed to claim a share in the mortgage security upon a parity with other bond and coupon holders.

Leaving aside the words "payment" and "purchase," neither of which aptly describes the situation, we are left with the simple question of whether or not the *method* of and the circumstances surrounding the paying agent's acquisition of matured bonds and coupons are such as to war-

rant denying him parity. No paying agent under the circumstances of this or any similar case would spend his funds to acquire mortgage bonds and coupons and so finance a default if he knew that the bonds and coupons so acquired would be deferred to the remaining ones in the hands of the public. Organizations placed in positions similar to that in which the American Bond & Mortgage Company found itself in the present case are entitled to a definite assurance as to whether or not they must give notice of their intention to claim parity for matured bonds and coupons which they acquire, and if notice is required, what sort of notice is sufficient. Such a definite assurance can be found, under the present conflicting state of the authorities, only in a pronouncement by this Court.

Where there is fraud or overreaching, of course parity will be denied. There was none in the present case. The Circuit Court of Appeals suggested no impropriety in the action of the American Bond & Mortgage Company. The furthest it went was to suggest that, if no requirement of notice of purchase was to be implied into the indenture, a situation would exist in which fraud might flourish (see Rec. pp. 112, 113). Unhappily, fraud may flourish in almost any situation. The question which we urge this Court to consider is whether this particular situation is one so susceptible to fraudulent practice that a party who has advanced large sums in entire good faith in reliance on indenture provisions which a District Judge has found could have no meaning unless they authorized what was done must forfeit them lest later some knave use its example for fraudulent purposes.

Until now the leading case on this question has been the decision of this Court in *Ketchum* v. *Duncan*, 96 U.S. 659, *supra*, but the decision of the Circuit Court of Appeals herein does not give proper effect to this Court's holding in that case. Mr. Justice Strong, speaking for the court, held

that intention was as much a requirement of a payment as it was of a sale. He said, at page 662:

> "It is as difficult to see how there can be a payment and extinguishment thereby of a debt without any intention to pay as it is to see how there can be a sale without an intention to sell."

The District Judge made no finding of the existence of an intention to pay on the part of the American Bond & Mortgage Company. On the contrary, he specifically found an intention not to pay but to purchase (Rec. p. 50). This finding was in no way disturbed by the Circuit Court of Appeals, but neither did that court give any effect to it. On the contrary, it wholly disregarded it. It is submitted, therefore, that the conclusion of the Circuit Court of Appeals that as a matter of law the acquisition of bonds and coupons by the American Bond & Mortgage Company was a payment, *i.e.*, was such a transaction as to prevent the securities acquired therein from being granted parity, did not give proper effect to so much of the decision of *Ketchum* v. *Duncan, supra,* as makes an affirmative intention by the paying agent a condition precedent to payment, with consequent subordination of matured bonds and coupons in his hands.*

Not only does the decision of the Circuit Court of Appeals in the present case fail to give proper effect to *Ketchum* v. *Duncan, supra,* and leaves the application of that case un-

**Ketchum* v. *Duncan* was relied on and followed by the Court of Appeals for the District of Columbia in *Lee* v. *Mitcham*, 98 F. (2d) 298, which presents a situation similar to that in the case at bar. The decision in that case on the point of assent cannot be reconciled with that in the instant one. In that case the court held there was a "purchase" of a note instead of "payment" where it was taken up without any actual notice to the holder that it was not to be discharged.

certain, but it is in apparent conflict with the decision of the Fifth Circuit in *Anderson* v. *Pennsylvania Hotel Co.*, 56 F. (2d) 980.

The Circuit Court, in its opinion in the present case, states (Rec. p. 112):

> "But we think that if the person making such a payment desires to exercise the option to treat the transaction as a purchase, he should manifest his intention to do so by some sort of notice to the coupon-holder, and he should disclose his intention at the time."

Such a requirement is something completely dehors the mortgage indenture but is implied by the court into the contract between the issuer and the bondholders. No such requirement of notice appeared in the indenture in the *Anderson* case, *supra*, and the court there granted parity to the bonds without requiring any proof of notice of intention to hold the bonds unsubordinated.

Furthermore, the *Anderson* case places the burden on the party opposing the claim of parity to show that, while some of his bonds were acquired by the paying agent, he held other bonds through to foreclosure and thereby would be harmed by a grant of parity to the paying agent. No such proof exists here. All the record shows (p. 31) is that—

> "Certain of the bonds acquired by American Bond & Mortgage Company and on which the plaintiff in this case asserts its rights were held at the time of such acquisition by persons who held other bonds of the same issue who later deposited these other bonds with the Committee."

All that the present respondents have proved, therefore, is that "certain" of the bondholders whose rights they have acquired will receive less if parity is accorded to the bonds

held by the petitioner. Moreover, there is absolutely nothing in the record to show that the "certain" bondholders suffered loss through postponement of foreclosure. They were quite content to take the paying agent's money and have never offered to return it. It did not appear that the properties fetched less on foreclosure than they would have fetched earlier. In the case of the Myles Standish the bid at the sale was the full amount of the indebtedness including the securities here in suit. It does appear that they will profit by parity being denied (they are the immediate recipients of the forfeiture), but that is a very different thing from a showing that they will suffer damage from parity being allowed. The decision of the Circuit Court of Appeals in denying parity to the petitioner in the absence of such proof of damage is in conflict with the decision of the Fifth Circuit in the *Anderson* case, *supra*. The existence of such a conflict, the petitioner asserts, further justifies the granting of the present petition for certiorari.

Turning to the applicable state cases, we again find the present decision of the First Circuit in irreconcilable conflict. In *Lyman* v. *Stevens*, 123 Conn. 591, the trustee under a corporate mortgage picked up matured bonds and coupons in pursuance of an indenture provision to the effect that the trustee might advance principal or interest not paid by the issuer and should thereupon to the extent of such advances be subrogated to the rights of the holders. This was done and the trustee was permitted to share in the security. While the court stated that the trustee (unlike the Mortgage Company here, an undoubted fiduciary) should have given notice that there was a default and that it proposed to seek subrogation for amounts advanced by it, it held that this was immaterial since it did not appear that the bondholders were in any way damaged by the trustee's failure to give such notice. As had been explained above in respect to the *Anderson* case, the requirement of proof

of damage marks a point of sharp conflict with the present decision.

Chicago Title & Trust Co. v. *Hoffberg*, 293 Ill. App. 290, 12 N.E. (2d) 230, is also irreconcilable with the present decision in that proof of ownership of other bonds and coupons by those objecting to parity was held essential.

The present decision, when viewed against the background of the prior judicial determinations on the subject which have been cited above, raises such sharp conflicts and leaves this branch of the law of corporate securities shrouded in such a mist of uncertainty that this Court, in the interest of promoting a uniformity of judicial decision and of clearly delimiting the rights and duties of those interested in or dealing with corporate securities, should grant the present petition.

III. The imposition of the forfeiture resulting from the decision below should be reviewed by this Court.

Although this Court in granting certiorari is properly concerned more with achieving uniformity of decision and practice than in correcting errors in particular decisions, miscarriage of justice must always be a pertinent and persuasive consideration. We present a grave miscarriage of justice on this record as an additional reason for granting the writ.

Bonds were sold by petitioner's predecessor, the Mortgage Company, to float wholly new ventures. Such "construction bonds" are notoriously a hazardous investment. They were conspicuously labelled "construction bonds" upon their face. They were issued under indentures which specifically provided that in the event of default by the issuer the Mortgage Company might purchase the bonds and coupons, hold them, and enforce them against the security. The Mortgage Company occupied no fiduciary

relationship which would disqualify it from making such a purchase.* There could be no possible objection, even had there been no indenture provisions, to a negotiated purchase and subsequent realization on the security. The issuer did default. The Mortgage Company advanced some $325,000 of its own money and took up the defaulted obligations. In so doing it acted in entire good faith, but it gave no notice that there was a default.† It did not intend to discharge or "pay" the obligations. The bondholders took its money quite happily. No offer has ever been made to return one penny of the money. It does not appear that any bondholder has suffered any damage by reason of this advance or would suffer any if parity is accorded to petitioner in the security. It does appear that all bondholders who took the Mortgage Company's money will necessarily profit by the transaction. Yet because the Mortgage Company failed to give notice that it intended to "purchase" rather than to donate its money and so to "pay," the Circuit Court of Appeals has enforced a forfeiture—and the cases are in equity.

Furthermore, this forfeiture has been enforced, not against the Mortgage Company itself, but against its creditors. The securities held by the petitioner, which the opinion of the Circuit Court of Appeals deprives of all value, it holds for the benefit of the creditors of the Mortgage Company. In *Lyman* v. *Stevens*, 123 Conn. 591, *supra*, a similar situation existed and was specially noticed by the

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*See *Hallett* v. *Moore*, 282 Mass. 380, and *Maryland Casualty Co.* v. *Moore*, 82 F. (2d) 189 (C.C.A. 1), which were cases in each of which endeavour was made to show identity between the trustee under the Pelham Hall mortgage and the Mortgage Company. In each case the endeavour was not successful.

†The District Judge in his opinion stated: "I have no doubt that the Mortgage Co., in financing these defaults, relied upon these provisions of the trust mortgages and believed it was incurring no risk in so doing" (Rec. p. 53).

court as an additional reason for refusing to impose a forfeiture.

On these facts we confidently assert that the petitioner has suffered an injustice. The question of law involved is one of general application in an important field of investment. An important point of practice is presented. We ask this Court to review the cases.

Respectfully submitted,

RICHARD WAIT,
CHARLES P. CURTIS, JR.,
JOHN DANE, JR.

INDEX.

TABLE OF AUTHORITIES CITED.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1940.

No. 506.

A. B. & M. LIQUIDATION CORPORATION,
PETITIONER,

v.

PELHAM HALL COMPANY ET AL.,
RESPONDENTS.

A. B. & M. LIQUIDATION CORPORATION,
PETITIONER,

v.

MYLES STANDISH COMPANY ET AL.,
RESPONDENTS.

BRIEF FOR THE RESPONDENTS, PELHAM HALL COMPANY, MYLES STANDISH COMPANY, FREDERICK G. CURRY AND WALTER J. SUGDEN, TRUSTEES, JAMES SUGDEN COMPANY, AND CATHERINE SUGDEN.

OPINIONS BELOW.

The opinion of the District Court is published in 28 F. Supp. 350. The opinion of the Circuit Court of Appeals is published in 112 F. (2d) 498. The petition for rehearing was denied without opinion.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered June 7, 1940. A petition for rehearing was filed in the Circuit Court of Appeals on June 21, 1940 and was

denied July 15, 1940. The petition for certiorari was filed October 14, 1940. The jurisdiction of this court is sought to be invoked under Section 240 (a) of the Judicial Code as amended.

QUESTIONS PRESENTED.

1. Whether or not a Circuit Court of Appeals may examine exhibits introduced in the District Court but not certified to the Circuit Court as a part of the record on appeal.

2. Where securities are issued under a trust mortgage providing that if the issuer fails to pay any bond or coupon secured by the mortgage the broker, which is also the paying agent, may purchase and hold such securities without these securities becoming subordinated to the other outstanding bonds and coupons of the same issue, and the broker or paying agent, in reliance upon that provision, takes up with its own money bonds and coupons as they fall due intending to purchase but without giving to the holders from whom such securities are taken up any notice of its intention to purchase, so that the holders believe that the bonds and coupons are being paid and not purchased, does that transaction constitute a purchase within the meaning of the provisions of the trust mortgage?

3. If on the facts stated in the preceding question, failure to give the notice there referred to does not constitute a purchase, does the presentation of a resale order with respect to bonds alone but not with respect to coupons constitute a notice on the part of the paying agent of its intention to exercise an option to purchase such bonds on its own account?

STATEMENT.

These two cases were brought by the A. B. & M. Liquidation Corporation, the plaintiff below, as transferee of the assets of the American Bond and Mortgage Company, Inc., to establish the parity of and its right to share in the security underlying coupons with a face value of approxi-

mately $114,000 and bonds with a face value of approximately $31,000 in the Pelham Hall case, and coupons with a face value of approximately $171,000 and bonds with a face value of approximately $62,000 in the Myles Standish case. The coupons and bonds came into the hands of the A. B. & M. Liquidation Corporation by virtue of a decree of the Bankruptcy Court for the Eastern District of Illinois dated July 20, 1934, entered in connection with a composition offer made by the American Bond and Mortgage Company in its bankruptcy proceedings. (Agreed statement of facts in the Pelham Hall case, R., p. 19, and in the Myles Standish case, R., p. 82.) These bonds were originally issued by a corporation known as The Pelham Hall, Inc. in the Pelham Hall case and by a corporation known as The Myles Standish, Inc. in the Myles Standish case. The indentures show that they were executed by the borrower and by a corporate trustee and an individual trustee. In addition to the actual parties to these indentures, the indentures throughout refer to the American Bond and Mortgage Company and make it the paying agent of the mortgagors for the sums coming due on coupons and principal maturities from time to time and also confer upon it certain rights and duties in connection with monthly instalments of interest, principal, and income taxes which under the indentures were to be paid to the American Bond and Mortgage Company as further security for the performance of the covenants under the indenture by the mortgagors. (R., pp. 39, 40, 44 and 45.) The indentures in each case also provided that the mortgaged property should be held for the equal protection of all the bonds and coupons. (R., pp. 39, 44 and 45.) The indentures also contained a provision which authorized the American Bond and Mortgage Company to purchase any coupon or bond which had not been paid on its due date and to hold that coupon or bond unsubordinated. (R., pp. 40 and 41.) It is these provisions in the

indentures upon which the plaintiff relies, and which were considered by the District Court and the Circuit Court of Appeals in drawing their conclusions of law. Both obligors failed to make the monthly payments required under the indenture. When the fifth coupon matured March 1, 1928, and subsequent ones matured September 1, 1928, and March 1, 1929, in the Pelham Hall case and the fourth coupon matured June 1, 1927, and subsequent ones came due December 1, 1927, June 1, 1928, and December 1, 1928, in the Myles Standish case, the American Bond and Mortgage Company had not been provided with funds to pay them. Nor were funds provided under either issue to meet the principal maturities which fell due in the Pelham Hall case on September 1, 1928 and March 1, 1929, or in the Myles Standish case on June 1, 1927, December 1, 1927, June 1, 1928 and December 1, 1928. Nonetheless, when these coupons and matured bonds were presented to the American Bond and Mortgage Company for payment, the American Bond and Mortgage Company, without any notice to the person presenting them, advanced from its own funds the face amount of these bonds and coupons. (Agreed statement of facts in the Pelham Hall case, paragraph 14, R., pp. 17 and 18, and in the Myles Standish case the agreed statement of facts, paragraph 11, R., pp. 79 through 81. For the finding as to the lack of notice to or knowledge of the persons presenting the coupons for payment, see the opinion of the District Court in paragraphs 2, 3, 4 and 5, R., pp. 48–50 incl.) The American Bond and Mortgage Company also paid the 2% Federal Tax due on the coupons so presented and taken up, and refunded to coupon holders the amount of State income taxes due. (R., p. 57.) In the Pelham Hall case, the first notice the bondholders had of any default was on August 22, 1929 when the American Bond and Mortgage Company so notified them, and this was notice *not of non-payment of past coupons but of a*

future coupon. (Paragraph 9 of the opinion of the District Court, R., pp. 42 and 43. As to the Myles Standish case, see paragraph 6 of the opinion, R., p. 46.) The respondent believes it important to point out that similar advances had been made in the Pelham Hall case for the coupons maturing March 1, 1927 and September 1, 1927, but the funds advanced for these coupons were repaid by the issuer and no question is raised as to them. (R., p. 17.) In the Myles Standish case, interest coupons due December 1, 1926 were paid from funds supplied by The Myles Standish, Inc. In both cases the coupons coming due in the first year were paid from funds reserved from the sale of bonds all as provided in the brokerage contracts. (See R., p. 16 in the Pelham Hall case and p. 79 in the Myles Standish case.)

Subsequent to the notices of default above referred to, the mortgages were foreclosed and eventually a plan of reorganization worked out with reference to each bond issue under which the mortgaged property was transferred in the Pelham Hall case to the Pelham Hall Company and in the Myles Standish case to the Myles Standish Company. The bondholders of The Pelham Hall, Inc. were given voting trust certificates representing shares of stock in the new company for their old bonds and coupons and the same procedure was followed in the Myles Standish case. The plans are briefly summarized in the opinion of the District Court. (R., pp. 43 and 47.)

The District Court opinion is found at pages 38 through 55 of the record. The District Court remarked that the decision depended upon the particular facts of the case (R., p. 51) and then discussed the indenture provisions, and, relying upon the fact that the bonds were construction bonds and that the indenture permitted the purchase of the coupons and bonds, concluded that the plaintiff should prevail. The opinion of the Circuit Court of Appeals is found

at pages 105 through 115 of the record. The Circuit Court of Appeals relied upon the fact that no notice of any description was given to the owners of the coupons and that the notice given to owners of the bonds which were presented for payment was given only after the actual presentation of the bond. The Circuit Court of Appeals also stressed the fact that the American Bond and Mortgage Company paid the Federal Income Tax due at the source on interest paid and refunded the State Income Tax due on interest paid to the holders of the coupons. (R., p. 108.) The Circuit Court then concluded (R., pp. 110 and 111) that the clause of the indenture relied upon by the district judge did not permit the American Bond and Mortgage Company to take up coupons and hold them unsubordinated without notice to the coupon holders. The Circuit Court arrived at the same conclusion with reference to matured bonds and further ruled that the so-called resale authorities were vague and indefinite in their terms and did not constitute adequate notice. The Circuit Court further relied on the fact that these notices, whatever may have been the proper interpretation of them, could not in any event serve as adequate notice because they were not given until after the bonds had been presented for payment. (R., p. 113.)

After the handing down of this decision, the petitioner filed motions for rehearing (R., p. 113) which were denied.

The petition in this court was filed on October 14, 1940.

With reference to the petitioner's statement of facts, the respondent respectfully calls the attention of this Court to the fact that in several instances the petitioner has used therein the words "purchase" and "payment". The question of whether or not the transaction constituted a purchase is the issue in the case and words assuming a conclusion should not be used. The petitioner on page 8 of its petition states that "the defendants other than the Boston Safe Deposit and Trust Company and the interveners ap-

peal." The interveners did appeal (R., pp. 59 and 101) and the materiality of this appeal will be discussed in this brief.

The petitioner on page 2 of its petition states that "except for the proceeds of the sale of these bonds neither corporation had any material resources." This is not a fact which appears in the record of these cases.

It must also be pointed out that although it may perhaps be inferred from the opinion of the Circuit Court of Appeals that at some time that court inspected the so-called resale authorities, there is nothing whatever in the record which justifies the statements made on page 8 of the petitioner's petition. So far as the record in this case is concerned, it does not appear (except as may be inferred from the language of the decision) that the Circuit Court of Appeals ever had in its possession the resale authorities, or if it did have them, when it had them, or what weight it gave to them.

SUMMARY OF ARGUMENT.

Certiorari should not be granted in this case because:

1. No important question of Appellate practice is involved in the inspection by the Circuit Court of Appeals of the resale authorities, because this inspection, if it were made, is authorized by Rule 75h of the Rules of Civil Procedure.

2. The decision of the Circuit Court of Appeals is not in conflict with any applicable decision of this Court or with the decision of another Circuit Court of Appeals or state court on the same matter, and no important question in the law of corporate securities is presented by the decision of the Circuit Court of Appeals, because its decision was based upon the facts as found by the district judge, and is strictly in conformity with the position of this Court in the case of *Ketchum* v. *Duncan,* 96 U.S. 659.

3. The decision of the Circuit Court of Appeals is not inequitable as causing the petitioner to be subjected to a forfeiture. The actions of the petitioner's predecessor by which the petitioner is bound were in themselves inequitable and any loss properly falls upon the petitioner and not upon the innocent holders of bonds and coupons.

ARGUMENT.

I.

The use by the Circuit Court of Appeals of an exhibit not incorporated in the formal record was proper. Whether in view of Rule 75 of the Rules of Civil Procedure the petitioner has any right to raise a question not appearing in the record may well be doubted. If, however, the petitioner may now properly raise the question of the propriety of the examination by the Circuit Court of Appeals of certain exhibits introduced in evidence before the District Court and not certified as a part of the record on appeal (if, in fact, the Circuit Court of Appeals did examine such exhibits), that question is answered by 75h of the Rules of Civil Procedure for the District Courts which provides in part as follows (italics supplied):

> "If anything material to either party is omitted from the record on appeal by error or accident or is misstated therein, the parties by stipulation, or the District Court, either before or after the record is transmitted to the Appellate Court, or the Appellate Court, on a proper suggestion or *of its own initiative, may direct that the omission or misstatement shall be corrected, and if necessary, that a supplemental record shall be certified and transmitted by the Clerk of the District Court.*"

The italicized portion of the above quotation answers fully the objection raised by the petitioner. There is no doubt that the resale authorities were introduced in evidence; in fact, they were introduced by the petitioner. The

petitioner was afforded every opportunity to interrogate with respect to them. The petitioner on page 16 of its petition cites the case of *Chisholm-Ryder Co.* v. *Buck*, 65 F. (2d) 735 (C.C.A. 4th Cir.). In that case the Circuit Court of Appeals examined a document which was not offered at the trial or introduced in evidence. The distinction between that case and the present case is obvious.

There is no formal order entered on the docket of the Circuit Court of Appeals instructing the Clerk of the District Court to transmit the resale authorities to the Circuit Court of Appeals but this is unnecessary in view of the provision in Rule 75h which does not *require* the certification of a supplemental record by the Clerk of the District Court but merely provides for such a supplemental record if necessary. It clearly lies within the discretion of the Circuit Court of Appeals to determine whether or not such formal certification is necessary. In the present case, it is obvious that the Circuit Court of Appeals did not consider it necessary.

Either the petitioner or the respondents could have included the resale authorities in the record on appeal. Neither party did so. The resale authorities were written documents and even though the petitioner may have omitted to argue their effect in the original hearing before the Circuit Court of Appeals, yet the petitioner must have assumed when the petition for rehearing was presented that the Circuit Court of Appeals had examined the resale authorities and at that time the petitioner had every opportunity to argue the proper construction of the resale authorities. The denial of the petition for rehearing justifies the assumption that the petitioner's arguments as to the resale authorities were insufficient to cause the Circuit Court of Appeals to alter its opinion.

If the Circuit Court of Appeals did direct that these exhibits be transmitted to it and if it did examine them, then

the Circuit Court of Appeals, acting under the authority conferred upon it by Rule 75h, did make the resale authorities a part of the record on appeal. If this was done after the filing of the briefs in the Circuit Court of Appeals and after the oral argument in that Court, although this does not appear as a matter of record, it was, in any event, done before the filing of the petitioner's motion for rehearing and the petitioner has therefore not been deprived of its opportunity to argue the sufficiency of the resale authorities.

Even if this court believes that the action of the Circuit Court of Appeals did not make the resale authorities a part of the record or that the certification of a supplemental record to include the resale authorities was a necessary procedure to be taken by the Circuit Court of Appeals, nevertheless, certiorari should not be granted in this case as the inspection of the resale authorities by the Circuit Court of Appeals did not affect its decision. The record as it originally stood and as presented to this Court discloses the manner in which the resale authorities were used. They were not used at all with respect to coupons and were not used by the holders of matured bonds when they were presented for payment. They were used only *after* a bond had been presented to American Bond and Mortgage Company, and then in some instances signatures were requested by that company from correspondent banks and in some instances from customers personally presenting their bonds for payment. (R., pp. 49, 113.) The Circuit Court of Appeals has stated clearly that the question as to whether the transaction constituted a purchase or payment was one to be determined at the time the bonds were presented for payment. The character of the transaction became irrevocably fixed when the bonds were presented. (R., p. 113.) The use by American Bond and Mortgage Company of a resale authority at some date subsequent to

the presentation of the bonds for payment even though closely following such presentation is insufficient. Therefore, whatever may have been the proper interpretation of the language of the resale authorities, the Circuit Court of Appeals has found they were not effective as notice because they were not given to any bondholders until after the time when the character of the transaction became fixed. (R., p. 113.) While it is true that the Circuit Court of Appeals characterized the resale blanks as "somewhat vague and technical in their terms" its decision was based primarily upon the fact that the use of the resale authorities was too late and it is obvious that the Circuit Court of Appeals would have reached the same decision whether or not it had inspected the resale authorities. It is, therefore, respectfully submitted by the respondents that whether or not the Circuit Court of Appeals erred in examining the resale authorities, if it did so, such error was not prejudicial to the petitioner.

II.

The basic question involved in the present litigation presents no problem of general concern to those interested in the ownership or flotation of corporate securities. The problem here presented is one of the construction of the language of particular indentures. The District Court properly so assumed (R. p. 51), as did the Circuit Court of Appeals. (R., p. 107.) The petitioner has relied upon that clause of the indentures, identical in both cases, which permitted the American Bond and Mortgage Company, the petitioner's predecessor, under certain circumstances to purchase bonds and coupons and to hold them unsubordinated. The only question is whether or not the American Bond and Mortgage Company did purchase within the meaning of that indenture clause. The Circuit Court of Appeals has held that upon the facts found by the district

court and appearing in the record, the American Bond and Mortgage Company did not purchase the bonds and coupons in litigation. That decision involves no problem in the law of corporate securities meriting any further adjudication. It is a matter wholly concerned with the interpretation of these particular indentures, and the acts done by the petitioner's predecessor. That this is true is clearly shown in the opinion of the Circuit Court of Appeals, as that court indicated that if the indentures had contained provisions similar to those in the indenture discussed in *Chicago Title & Trust Co.* v. *Hoffberg,* 293 Ill. App. 290, 12 N.E. (2d) 230, a different result might well have been reached. (R., p. 111.) The problem presented in the present cases is not one of purchase or payment but merely whether or not a purchase was made under the provisions of these indentures. "Purchase" or "payment" are not necessary alternatives. The Circuit Court of Appeals in holding that the American Bond and Mortgage Company was not in the position of a purchaser of the coupons and bonds here involved did not hold they were paid, nor need it have done so.

The petitioner argues that the decision of the Circuit Court of Appeals failed to give proper effect to *Ketchum* v. *Duncan,* 96 U.S. 659. On the contrary the Circuit Court of Appeals considered the case of *Ketchum* v. *Duncan* with great care, quoted, extensively from its language (R., pp. 109, 110) and found expressly that the facts of the present cases were quite different. The Circuit Court of Appeals said in that respect (R., p. 110):

> "The payment of the coupons in the Duncan case was held not to extinguish them because the circumstances of that case warranted the presumption 'that both parties supposed and expected that the coupons remaining uncancelled would be preserved and held as claims against the railroad company'. The circumstances here are quite different. The District Court

found that the coupons were 'paid at the place they were to be paid and by the party who was to pay them and were paid at approximately the time when they should have been paid; that they were paid without notice to the holder or person presenting them that they were being purchased.'

"No notice was given to the holders of the securities of any purpose on the part of the Mortgage Company to purchase and nothing occurred which 'should have awakened their attention and led them to inquire.' Every appearance of purchase was avoided. The natural belief from all the circumstances that the coupons were being paid and not purchased was also encouraged by the fact that the Mortgage Company paid the necessary state and federal income taxes, which are only payable when interest is being paid and not when interest coupons are bought and sold."

Not only is it true that the facts in *Ketchum* v. *Duncan* were dissimilar to those in the instant cases, but the reasoning of this Court in *Ketchum* v. *Duncan* when applied to the facts of the present cases leads to the same result arrived at by the Circuit Court of Appeals. The decision of the Circuit Court of Appeals does not leave the application of *Ketchum* v. *Duncan* uncertain.

The petitioner also claims that there is an apparent conflict between the decision of the Circuit Court of Appeals for the Fifth Circuit in the case of *Anderson* v. *Pennsylvania Hotel Co.*, 56 F. (2d) 980 and the decision of the Circuit Court of Appeals in the present cases. In the first place, there can be no conflict between the two decisions in so far as coupons are concerned as the *Anderson* case involved only matured bonds and did not involve coupons. In *Anderson* v. *Pennsylvania Hotel Co.* the court recognized that the case of coupons differed from the matured bonds which were under consideration in that case because the holder of coupons which have been taken up remains interested in the security underlying the other coupons and bonds which he owns. (*Anderson* v. *Pennsylvania Hotel*

Co., 56 F. (2d) 980, at 983.) Secondly, with respect to matured bonds the basis of the decision in the *Anderson* case is that it did not appear in that case that any person whose bond was taken up had any further interest in the security or held any other bonds of the same issue. In the instant cases, the interveners were holders of other bonds of the same issue and they were permitted to intervene not only on their own behalf but on behalf of other bondholders, many of whom held other bonds of the same issue. (R. pp. 24, 25, 31, 86, 87, and 93.) This obvious factual difference is a fundamental distinction between the present decision and the Anderson decision and there is no apparent or actual conflict with respect to the problems of law decided by the two Circuit Courts of Appeals. Furthermore, the requirement of notice stated by the Circuit Court of Appeals in its opinion in the present case and set out on page 21 of the petitioner's brief in support of its petition is not a requirement *dehors* the mortgage indenture or implied by the contract between the issuers and the bondholders. It must be remembered that the petitioner is seeking to establish its right as assignee from a purchaser and it is therefore clearly encumbent upon the petitioner's assignor to do those things necessary legally to constitute a purchase. Adequate notice of intention to purchase is clearly a necessary requisite.

The decision in *Lyman* v. *Stevens,* 123 Conn. 591 is not in irreconcilable conflict with the decision of the first circuit. Rather the two cases are entirely consistent. The mortgage indenture in *Lyman* v. *Stevens* contained a provision allowing the indenture trustee to advance principal or interest not paid by the issuer and specifically provided that the trustees should be subrogated to the rights of the bondholders to the extent of such advances. The trustee therein was given a right to make advances, not merely a right to purchase.

Chicago Title and Trust Co. v. *Hoffberg,* 293 Ill. App. 290 is also wholly consistent with the present decision. As has been pointed out above in the respondents' brief and as the Circuit Court of Appeals itself recognized (R., p. 111) the indenture clause with which the court was concerned in *Chicago Title and Trust Co.* v. *Hoffberg* specifically provided that if the trustee bank advanced its own funds for bonds or coupons, such bonds or coupons "shall thereupon be deemed to have been purchased . . . and it shall be unnecessary to give notice of any such purchase to the mortgagor or to the holders of other bonds or coupons secured hereby or to anyone else. . . ."

The requirement of the *Hoffberg* case of proof of ownership of other bonds and coupons by those objecting to parity is fully met by the respondents in the present cases. (R., pp. 24, 25, 21 and 86, 87, 93.)

Far from there being any mist of uncertainty arising from the present decision, the almost uniform course of decisions of both state and United States courts has been to deny parity to bonds and coupons taken up in a manner similar to the method used in the present cases, in the absence of unusual circumstances such as were found to exist in *Ketchum* v. *Duncan, supra,* and *Anderson* v. *Pennsylvania Hotel Co., supra,* and in the absence of such unusual indenture provisions as were contained in *Chicago Title and Trust Co.* v. *Hoffberg, supra.* The following are cases which conclusively demonstrate that the decision of the Circuit Court of Appeals in the present cases is in accord with the uniform course of decisions.

Wood v. *Guaranty Trust Company,* 128 U.S. 416.

Ferree v. *New York Security & Trust Company,* 74 Fed. 769 (C.C.A. 8th).

Farmers Loan & Trust Co. v. *Iowa Water Co.,* 78 Fed. 881.

Venner v. *Farmers Loan and Trust Co. of New York*, 90 Fed. 348 (C.C.A. 6th).

First Trust Company of Lincoln, Nebraska v. *Ricketts*, 75 F. (2d) 309 (C.C.A. 8th).

Martin v. *Bank*, 94 Tenn. 176, 28 S.W. 1097.

Morton Trust Company v. *Home Telephone Company*, 66 N.J.Eq. 106, 57 Atl. 1020.

Baker v. *Meloy*, 95 Md. 1, 51 Atl. 893.

Union Trust Company v. *Monticello & Port Jervis Railway Co.*, 63 N.Y. 311.

Lloyd, Trustee v. *Wagner*, 93 Ky. 644, 21 S.W. 334.

Security Trust Company v. *American Investment Company*, 34 N.M. 551, 286 Pac. 159.

Lake View Trust & Savings Bank v. *Joseph P. Rice*, 279 Ill. App. 538.

Tracy, Corporate Foreclosures (1929) s. 253.

Cook on Corporations (8th Ed.) s. 771.

McLelland and Fisher, "Law of Corporate Mortgage Bond Issues" (1937) p. 508.

III.

The decision below does not result in an imposition of a forfeiture. The petitioner claims that on the record there is a grave miscarriage of justice justifying this court in granting a writ of certiorari. It is clear in the first place that the petitioner can stand in no better position than its assignor, the American Bond and Mortgage Company.

The petitioner refers at some length to the good faith of American Bond and Mortgage Company and to the fact that the bonds were labelled "construction bonds" upon their face. In so arguing the petitioner overlooks the fact that the first year's instalments of interest were withheld by American Bond and Mortgage Company from the proceeds of the sale of the bonds and also overlooks the fact that there were no early maturities of principal. (R., pp. 16,

79.) The first principal maturity in either case was two years after the date of the bond issue.

The petitioner reminds the Court that these cases are in equity. Therefore the findings of the Circuit Court of Appeals that when the American Bond and Mortgage Company took up maturing bonds and coupons without notice that they were being paid from funds supplied by the mortgage company "it was obviously to the advantage of the mortgage company not to disclose the true situation as it was dealing in these very bonds and also selling its own debentures" (R., p. 107) is properly a matter to be considered upon any claim of forfeiture. The Circuit Court of Appeals also stated "in the absence of language dispensing with notice, a construction is justified and called for which lends protection to the purchaser of securities and tends to reduce the opportunities for sharp practice and deceit in such transactions where knowledge of pertinent facts is withheld from the public." (R., p. 112.) If anything further need be said with respect to the relative equities involved, the language of the district court is pertinent. "Obviously the mortgage company was not advertising the fact that these bonds were in default. Its business was selling such real estate bonds." (R., p. 50.) The statements of the petitioner on page 24 of its brief in support of its petition that "The bondholders took its money quite happily. No offer has ever been made to return one penny of the money," are entirely unwarranted by anything that appears in the record. It is an agreed fact that the interveners in these cases held other bonds of these issues and as a result of reorganization now hold voting trust certificates representing these bonds. (R., pp. 31, 93.) The judge of the district court found it to be a fact that many of the bondholders whose matured bonds and coupons were paid were holders of bonds at the time of the foreclosure and participated in the plan of reorgani-

zation. (R., p. 50.) It is obvious that if the petitioner is permitted to prevail the proportionate holdings of the interveners and other stockholders will be greatly reduced and the value of their holdings correspondingly decreased. There is no reason why such a loss to the former bondholders who are now stockholders would not be as much a forfeiture as for the loss to remain where it is. As has been pointed out, the motives of the American Bond and Mortgage Company in acquiring these bonds and coupons were not entirely disinterested. The American Bond and Mortgage Company was dealing in these very bonds and selling its own debentures (R., p. 107) and the American Bond and Mortgage Company had an interest in concealing the failure of the mortgagor to meet its obligations. (R., p. 52.) With reference to the Pelham Hall case, the American Bond and Mortgage Company owned all of the stock of the issuer. (R., p. 15.) Nor, as has been pointed out, can the present petitioner stand in any better position than its assignor, the American Bond and Mortgage Company.

Carson v. *Nuzman,* 117 Kan. 395, at 397, 232 Pac. 242.

That there will be less for the creditors of American Bond and Mortgage Company because of the decision of the Circuit Court of Appeals than there would have been if the bonds and coupons in issue were allowed to participate in the reorganizations upon a parity with the bonds held by the public may be unfortunate for those creditors, but to grant such parity would be unfortunate for the bondholders who acted in good faith and believed that the bonds and coupons presented by them to American Bond and Mortgage Company had been paid.

The word "forfeiture" as used by the petitioner is hardly accurate. The petitioner still has a legal right against the original issuers of these bonds and coupons. The decision does not hold that these bonds and coupons are

paid with respect to the original issuers and whether this remedy of the petitioner against the original issuers will result in a substantial recovery or in no recovery at all is not material. When there is a remedy, even though that remedy may be against a worthless debtor, there is no forfeiture. Had the original issuers succeeded in repaying to American Bond and Mortgage Company the amounts it advanced, as in fact was done with respect to two maturities of coupons so taken up (R., p. 17) there would have been no complaint. The cry of forfeiture is now raised only because American Bond and Mortgage Company over-estimated the ability of the original issuers of these bonds to earn money and thus reimburse American Bond and Mortgage Company.

In several cases involving similar facts the courts have said that the remedy of the person picking up the coupons is not a right to share in the security on a parity with the innocent holders of bonds and coupons but is a right to come in ahead of general creditors or junior lienors.

Allyn v. *Dreher,* 124 Neb. 342, 246 N.W. 731.
Atherton v. *Tesch,* 202 Ala. 448, 80 So. 832.
Carson v. *Nuzman,* 117 Kan. 395, 232 Pac. 242.

CONCLUSION.

The respondent respectfully urges that the petition for certiorari be denied in view of the facts that:

1. Petitioner has not adduced any authority which casts doubt upon the correctness of the decision of the Circuit Court of Appeals.

2. No conflict of authority is shown to be involved nor is any novel question of law presented.

Respectfully submitted,

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